APPENDIX FOR PETITIONERS

# Supreme Court of The United States

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No.

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DARLINGTON-HARTSVILLE COCA-COLA BOTTLING COMPANY, INC., *Petitioner*

*versus*

UNITED STATES OF AMERICA, *Respondent*

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No.

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SPARTANBURG COCA-COLA BOTTLING CO., *Petitioner*

*versus*

UNITED STATES OF AMERICA, *Respondent*

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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
SPARTANBURG DIVISION

Civil Action No. 66-320

Darlington-Hartsville Coca-Cola Bottling Company, Inc., Plaintiff

v.

United States of America, Defendant

Civil Action No. 66-330

Spartanburg Coca-Cola Bottling Co., Plaintiff

v.

United States of America, Defendant

ORDER

This matter has been submitted to the Court for a determination upon the basis of written briefs presented on behalf of the parties to these actions. The facts of the case have been stipulated and the stipulation is hereby incorporated and made a part of this Order by reference as being an accurate statement of the factual situation surrounding this case.

The sole issue is whether the payments made by the plaintiff bottling companies on January 8, 1964, to The Coca-Cola Company are deductible by the plaintiffs as ordinary and necessary business expenses under Sec. 162 (a) of the Internal Revenue Code of 1954.

The plaintiffs argue that these payments were made solely to eliminate burdensome and onerous contracts and are, therefore, deductible as ordinary and necessary business expenses. In support of this contention, the plaintiffs cite the following authorities: *Stuart Co. v Commissioner,* 9 TCM 585 (1950), aff'd 195 F.2d 176 (9th Cir. 1952); *Pressed Steel Car Co. v Commissioner,* 20 TC 198 (1953), acq. 1956-2 CB 8; *Bressner Radio, Inc. v Commissioner,* 28 TC 378 (1957), acq. 1958-1 CB 4, rev'd and rem'd on other grounds 267 F. 2d 520 (2d

Cir. 1959); Appeal of Denholm & McKay Co., 2 BTA 44 (1925), acq. IV-2 CB 2; *Helvering v Community Bond & Mfg. Co.*, 74 F. 2d 727 (2d Cir. 1935), aff'g 27 BTA 480; *Montana Power Co. v United States*, 171 F. Supp. 943 (Ct. Cls. 1959); and *Metropolitan Co. v United States*, 176 F. Supp. 195 (S.D. Ohio 1959).

On the other hand, the Government takes the position that these payments were for the purpose of acquiring new and more favorable franchise bottling contracts and, therefore, constitute capital expenditures which are not deductible as ordinary and necessary business expenses. *Welch v Helvering*, 290 U.S. 111 (1933); Sec. 263 of the Internal Revenue Code of 1954.

Regardless of whether these payments were for new and more favorable contracts as the Government contends or for the elimination of burdensome and onerous contracts as the plaintiffs contend, the ultimate purpose and effect of these payments is clear. They were part of a well thought out three part plan to improve the profits of the bottling company plaintiffs by eliminating a non-productive middle man's contract, thereby reducing the base prices for syrup paid by the plaintiffs by making possible direct and more favorable contracts with the Coca-Cola Company which were subsequently negotiated.

The general rule is that an expenditure is a capital outlay, as opposed to an ordinary and necessary business expense, if it brings about the acquisition of a business advantage extending into the indefinite future. *United States v Akin*, 248 F. 2d 742 (10th Cir. 1957). This principle has been applied in this Circuit. "A taxpayer may, therefore, not deduct as a current business expense the full cost of acquiring an asset, tangible or intangible, which benefits the taxpayer for more than one year." *Richmond Television Corp. v United States*, 345 F. 2d 901, 907 (4th Cir. 1964).

The purpose of this rule is clear. Our income taxation is a plan to match the income and expenses of a given taxable year so as to tax only that which is net income. An expense which results in the acquisition of even an intangible business

advantage which benefits the taxpayer for more than one year, therefore, may not be deducted as a current business expense.

These January 8, 1964, payments by the plaintiffs secured for them a business advantage which extends into the indefinite future. Even though the payments were made only once and were nonrecurring. The benefits gained by virtue of these payments could reasonably be expected to continue for an indefinite time. Indeed, they have already survived the accounting period for which the business deduction is claimed.

The Court realizes that the expenditure does not have to be recurrent, does not have to be an absolute necessity, and does not have to be involuntarily made in order to qualify for a business deduction. The Court further understands that each case must be considered under its own peculiar facts and that in this case no actual physical assets were obtained. Nevertheless, the Court concludes that these payments constitute capital expenditures not deductible as ordinary and necessary business expenses since they obtained for the plaintiffs an intangible business advantage of an indefinite duration which extends beyond the accounting period for which the deduction is claimed, and into the indefinite future. It must be concluded that the plaintiffs are not entitled to refunds. Accordingly,

IT IS ORDERED that judgment be entered in favor of the defendant, the United States of America.

Columbia, S.C.
May 1967

s/J. Robert Martin, Jr.
United States District Judge

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 11,664

Darlington-Hartsville Coca-Cola Bottling Company, Inc.,
Appellant,

*Versus*

United States of America,
Appellee.

No. 11,665

Spartanburg Coca-Cola Bottling Co.,
Appellant,

*versus*

United States of America,
Appellee.

Before Haynsworth, Chief Judge, and Bryan and Butzner, Circuit Judges.

Albert V. Bryan, Circuit Judge:

Taxpayers, Darlington-Hartsville Coca-Cola Bottling Company, Inc. (Darlington) and Spartanburg Coca-Cola Bottling Company (Spartanburg), appeal the District Court's decision that certain payments made by them to the Coca-Cola Company (Coca-Cola) in 1964 were correctly characterized by the Commissioner of Internal Revenue as capital expenditures. We affirm.

In outline the facts are these. The payments were made as part of a plan to eliminate an unwanted middleman in the distribution of Coca-Cola syrup. For many years the middleman, H.D. and J. K. Crosswell, Inc. (Crosswell) had exclusive rights to bottle the syrup as the Coca-Cola beverage in specified areas of South Carolina. Under this agreement, Crosswell bought syrup at a set price per gallon, and was empowered

with the approval of Coca-Cola to grant bottling privileges to other (second-line) companies. As Crosswell second-liners, taxpayers were entitled to put up the beverage with syrup from Crosswell. Spartanburg and Darlington gave Crosswell more for this syrup than it had paid Coca-Cola, but Crosswell did almost nothing in dispensing the commodity.

Feeling the pinch of competition, the Coca-Cola Company and taxpayers decided to be rid of Crosswell so they could buy syrup at a lower figure. Under a negotiated plan, Coca-Cola purchased Crosswell's capital stock and liquidated the corporation. Taxpayers then reimbursed Coca-Cola for the stock acquisition, and in exchange were awarded contracts to obtain syrup at a price not dearer than was charged Crosswell.

Taxpayers deducted the amount of reimbursements as ordinary and necessary business expense. Int. Rev. Code of 1954, §162. With the deduction disallowed, the deficiency assessed and paid, this suit for refund followed.

The District Judge was of the same mind as the Commissioner upon the capital nature of the reimbursement. We concur, and adopt the judge's opinion save in its possible implication that a payment merely to be rid of "burdensome and onerous contracts" is per se a capital layout. Presumably, every such payment would bring a correlative advantage — relief from the burden — but this alone would not turn the money into capital. See Pressed Steel Car Co., 20 T.C. 198 (1953), *acq.* 1956-2 Cum. Bull. 1; Cleveland Allerton Hotel v. Commissioner, 166 F2d 805 (6 Cir. 1948).

What does distinguish a capital expenditure, in this respect, is its intendment to produce a positive business benefit whose effects will be reaped in seasons beyond a single year. Richmond Television Corp. v. United States, 345 F2d 901 (4 Cir. 1965); United States v. Akin, 248 F2d 742, 744 (10 Cir. 1957); see 4 A. Mertens, Federal Income Taxation §25.20 (1966). Taxpayers' outlays were designed to procure a less costly Coca-Cola syrup. The contracts thus obtained were of indefinite duration, and were contrived to better the profits over the years to come. For this reason, in addition to the

others arrayed by the District Court, each taxpayer's undertaking became a capital investment.

*Affirmed.*

## OPINION ON PETITION FOR REHEARING

Albert V. Bryan, Circuit Judge:

In a petition for rehearing petitioners cited instances where deductions have been allowed even though the taxpayer acquired through the expenditure in question an advantage the useful life of which extended into the indefinite future. It should be noted, however, that in the examples cited, the advantage acquired bore a close analogy to a "wasting" asset. Though its useful life extended into the indefinite future, it was reasonable to assume that at some point its life would come to an end. See *Amortization of Intangibles: An Examination of the Tax Treatment of Purchased Goodwill,* 81 Harv. L. Rev. 859 (1968). This "wasting" characteristic distinguishes the examples cited from the advantage acquired in the instant ease. Here, it is reasonable to view the advantage acquired as having an unlimited useful life, and petitioner has made no showing to the contrary. Where the benefit derived from an expenditure cannot be expected to cease, it would seem inappropriate to grant a deduction either currently or amortized over a period of years.

For these reasons the petition for rehearing will be denied.

## STIPULATION OF FACTS

(Full Stipulation set out in Appendix to Respondent's Brief to Court of Appeals at pps. 24-34)

(10) During 1963, most of the bottling companies having contracts with Crosswell, Inc. and Estate entered into negotiations among themselves and with The Coca-Cola Company to develop some plan whereby such bottling companies could purchase Coca-Cola syrup at more favorable prices. Other carbonated soft drinks by that time were competing strenuously with Coca-Cola and had reduced Coca-Cola's share of the carbonated soft drink market. Because of competition from

other soft drinks, The Coca-Cola Company during the period following World War II commenced marketing Coca-Cola in several different packages which increased Plaintiffs' expense of doing business. Therefore, The Coca-Cola Company was interested in consolidating and upgrading its bottling companies in order to improve their profits and thereby promote its own interests.

The bottling companies and The Coca-Cola Company decided that elimination of Crosswell, Inc. and its contracts would be one way to make it possible for the bottling companies to buy Coca-Cola syrup at more favorable prices. The stockholders of Crosswell, Inc. refused to consider a sale of their Crosswell, Inc. stock to the separate bottling companies but agreed to sell their stock to The Coca-Cola Company. Therefore, the bottling companies and The Coca-Cola Company agreed upon the following plan:

> (a) The Coca-Cola Company would purchase the stock and liquidate Crosswell, Inc.
>
> (b) The bottling companies would then reimburse The Coca-Cola Company for the purchase price of the Crosswell, Inc. stock.
>
> (c) Simultaneous with the reimbursement, the Crosswell, Inc. contracts would be surrendered and The Coca-Cola Company would replace them with contracts setting the base price of syrup at $1.30 per gallon.

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(14) The contracts dated January 8, 1964, did not alter in any degree the geographic areas specified in the earlier contracts or the provisions governing the bottling and sale of Coca-Cola in the respective geographic areas. They, however, did reduce the base price of Coca-Cola syrup to Spartanburg from $1.40 to $1.30 per gallon, and to Darlington from $1.50 to $1.35 per gallon.